

COSTA MESA SANITARY DISTRICT

Financial Statements

Year ended June 30, 2003

(With Independent Auditors' Report Thereon)

COSTA MESA SANITARY DISTRICT

Financial Statements

Year ended June 30, 2003

(with comparative totals for the year ended June 30, 2002)

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Board of Directors
Costa Mesa Sanitary District
Costa Mesa, California

Independent Auditors' Report

We have audited the accompanying financial statements of the business-type activities, each major fund and the aggregate remaining fund information of the Costa Mesa Sanitary District ("District") as of and for the year ended June 30, 2003, which collectively comprise the District's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of the Costa Mesa Sanitary District's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities, each major fund and the aggregate remaining fund information of the Costa Mesa Sanitary District as of June 30, 2003 and the respective changes in financial position and cash flows, where applicable, of the Costa Mesa Sanitary District for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed further in the notes to the basic financial statements, the accompanying financial statements reflect certain changes in the presentation of financial data required as a result of the implementation of GASB Statement No. 34 for the year ended June 30, 2003.

The information identified in the accompanying table of contents as *management's discussion and analysis* is not a required part of the basic financial statements, but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Board of Directors
Costa Mesa Sanitary District
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Our audit was made for the purpose of forming an opinion on the financial statements that collectively comprise the Costa Mesa Sanitary District's basic financial statements. The combining nonmajor fund financial statements listed in the table of contents as supplementary schedules are presented for purpose of additional analysis and are not a required part of the basic financial statements. The combining nonmajor fund financial statements have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Conrad and Associates, L.L.P.

September 22, 2003

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion and analysis of the financial performance of the *Costa Mesa Sanitary District* ("the District") provides an overview of the District's financial activities for the fiscal year ended June 30, 2003. Please read it in conjunction with the financial statements identified in the accompanying table of contents.

INFORMATION REPORTED IN THE ACCOMPANYING FINANCIAL STATEMENTS

One of the most important questions asked about the District's finances is, "Is the District better off or worse off as a result of the year's activities?" The Statement of Net Assets and the Statement of Revenues, Expenses, and Changes in Net Assets report information about the District in a way that helps answer this question. These statements include all assets and liabilities using the *accrual basis of accounting*, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

The financial statements of the District report the District's net assets and changes in them. You can think of the District's net assets – the difference between assets and liabilities –as one way to measure the District's financial health, or *financial position*. Over time, *increases and decreases* in the District's net assets are one indicator of whether its *financial health* is improving or deteriorating.

This financial report is designed to provide our citizens, customers, and creditors with a general overview of the District's finances and to show the District's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the District Office, at 77 Fair Drive, Costa Mesa, California, 92628.

CAPITAL ASSETS

Capital activity of the District for the year ended June 30, 2003 was limited to acquisition of equipment in the amount of \$98,350 and construction of District related facilities in the amount of \$130,123. \$86,982 of this construction related to Project No. 990024 for water service lines.

LONG-TERM DEBT

The District's long-term debt is limited to a capital lease entered into on July 12, 2001, with the Municipal Finance Corporation to provide financing in the amount of \$2,200,000 for the acquisition of refuse containers. Debt activity during the year was limited to principal repayments of \$179,376.

DISTRICT FINANCIAL STATEMENTS

The following should be noted with respect to the data presented in the District financial statements. During the year ended June 30, 2003, the financial condition of the District improved as indicated by the increase in the District's equity by the amount of \$63,251. This represents the excess of revenues earned by the District over its expenses incurred for the year ended June 30, 2003. For the year ended June 30, 2003, operating revenues were 6.1% higher than the prior year. Operating expenses for the year ended June 30, 2003 were 4.3% greater than the prior year. This increase was primarily due to increases in dump charges and solid waste and liquid waste disposal costs. These increases in operating expenses were somewhat offset by reduced outlays for sewer maintenance activities for the current year compared to the prior year. Because of declines in interest rates available in the investment market, investment earnings was 21.3% less than the prior year.

A summary of the District's financial statements on a consolidated basis follows.

Management's Discussion and Analysis
Change in Consolidated Statement of Net Assets
June 30, 2003 and 2002

	2003	2002	Change
<u>Assets</u>			
Current assets:			
Cash and investments	\$ 11,368,377	10,634,349	734,028
Cash with fiscal agent	-	248,939	(248,939)
Accounts receivable	508	2,962	(2,454)
Interest receivable	58,732	68,152	(9,420)
Taxes receivable	107,671	107,271	400
Due from other governments	4,957	12,910	(7,953)
Total current assets	<u>11,540,245</u>	<u>11,074,583</u>	<u>465,662</u>
Capital assets:			
Property rights	4,025	4,025	-
Subsurface sewer lines	19,914,147	19,914,147	-
Buildings and improvements	346,520	346,520	-
Equipment	2,750,085	2,651,735	98,350
Construction in progress	430,134	300,011	130,123
Total capital assets	<u>23,444,911</u>	<u>23,216,438</u>	<u>228,473</u>
Less accumulated depreciation	<u>(11,017,532)</u>	<u>(10,420,389)</u>	<u>(597,143)</u>
Net capital assets	<u>12,427,379</u>	<u>12,796,049</u>	<u>(368,670)</u>
Total assets	<u>23,967,624</u>	<u>23,870,632</u>	<u>96,992</u>
<u>Liabilities and Net Assets</u>			
Current liabilities:			
Accounts payable	493,712	542,278	(48,566)
Accrued liabilities	2,636	3,640	(1,004)
Interest payable	31,720	-	31,720
Deposits payable	3,067	11,619	(8,552)
Due to other governments	308,661	69,142	239,519
Due to the City of Costa Mesa	1,000	1,000	-
Capital lease payable	188,309	179,376	8,933
Total current liabilities	<u>1,029,105</u>	<u>807,055</u>	<u>222,050</u>
Long-term liabilities:			
Capital lease payable	1,745,844	1,934,153	(188,309)
Total long-term liabilities	<u>1,745,844</u>	<u>1,934,153</u>	<u>(188,309)</u>
Total liabilities	<u>2,774,949</u>	<u>2,741,208</u>	<u>33,741</u>
Net assets:			
Invested in capital assets, net of related debt	10,493,226	10,682,520	(189,294)
Restricted for capital outlay	2,406,728	3,582,907	(1,176,179)
Unrestricted, available for appropriations	8,292,721	6,863,997	1,428,724
Total net assets	<u>\$ 21,192,675</u>	<u>21,129,424</u>	<u>63,251</u>

Management's Discussion and Analysis

Change in Statement of Revenues, Expenses and Changes in Fund Net Assets

Year ended June 30, 2003 and 2002

	2003	2002	Change
Operating revenues:			
Trash assessments	\$ 4,105,544	3,884,972	220,572
Sewer assessments	1,642,255	1,571,722	70,533
Permits and inspection fees	43,126	34,820	8,306
Connection fees	44,230	53,979	(9,749)
Other services	61,726	-	61,726
Investment recovery	2,332	12,967	(10,635)
	<u>5,899,213</u>	<u>5,558,460</u>	<u>340,753</u>
Total operating revenues			
Operating expenses:			
Solid waste disposal	2,356,566	2,289,609	66,957
Liquid waste disposal	906,596	854,911	51,685
Dump charges	1,927,050	1,756,721	170,329
Other	499,118	672,241	(173,123)
Depreciation	597,144	450,943	146,201
	<u>6,286,474</u>	<u>6,024,425</u>	<u>262,049</u>
Total operating expenses			
Operating income (loss)	<u>(387,261)</u>	<u>(465,965)</u>	<u>78,704</u>
Non-operating revenues (expenses):			
Investment income	418,691	531,421	(112,730)
Interest expense	(133,526)	(54,120)	(79,406)
Taxes	165,347	150,214	15,133
Other revenues (expenses)	-	3,083	(3,083)
	<u>450,512</u>	<u>630,598</u>	<u>(180,086)</u>
Total non-operating revenues (expenses)			
Income before capital contributions	<u>63,251</u>	<u>164,633</u>	<u>(101,382)</u>
Contributions:			
Contributed capital assets	-	131,680	(131,680)
	<u>-</u>	<u>131,680</u>	<u>(131,680)</u>
Total contributions			
Net income	63,251	296,313	(233,062)
Net assets at beginning of year, as restated	<u>21,129,424</u>	<u>20,833,111</u>	<u>296,313</u>
Net assets at end of year	<u>\$ 21,192,675</u>	<u>21,129,424</u>	<u>63,251</u>

BASIC FINANCIAL STATEMENTS

COSTA MESA SANITARY DISTRICT
Enterprise Funds
Statement of Net Assets
June 30, 2003
(with comparative totals as of June 30, 2002)

			Nonmajor Enterprise Funds	Totals	
	Solid Waste	Liquid Waste		2003	2002
<u>Assets</u>					
Current assets:					
Cash and investments (note 2)	\$ 1,829,711	7,145,423	2,393,243	11,368,377	10,634,349
Cash with fiscal agent (note 2)	-	-	-	-	248,939
Accounts receivable	304	204	-	508	2,962
Interest receivable	9,438	36,956	12,338	58,732	68,152
Taxes receivable	89,158	18,513	-	107,671	107,271
Due from other governments	-	3,810	1,147	4,957	12,910
Total current assets	1,928,611	7,204,906	2,406,728	11,540,245	11,074,583
Capital assets:					
Property rights	-	4,025	-	4,025	4,025
Subsurface sewer lines	-	19,597,726	316,421	19,914,147	19,914,147
Buildings and improvements	-	346,520	-	346,520	346,520
Equipment	2,291,360	458,725	-	2,750,085	2,651,735
Construction in progress	-	430,134	-	430,134	300,011
Total capital assets	2,291,360	20,837,130	316,421	23,444,911	23,216,438
Less accumulated depreciation	(146,201)	(10,844,963)	(26,368)	(11,017,532)	(10,420,389)
Net capital assets	2,145,159	9,992,167	290,053	12,427,379	12,796,049
Total assets	4,073,770	17,197,073	2,696,781	23,967,624	23,870,632
<u>Liabilities and Net Assets</u>					
Current liabilities:					
Accounts payable	228,817	264,895	-	493,712	542,278
Accrued liabilities	1,831	805	-	2,636	3,640
Interest payable	31,720	-	-	31,720	-
Deposits payable	200	2,867	-	3,067	11,619
Due to other governments	-	308,661	-	308,661	69,142
Due to the City of Costa Mesa	500	500	-	1,000	1,000
Capital lease payable (note 6)	188,309	-	-	188,309	179,376
Total current liabilities	451,377	577,728	-	1,029,105	807,055
Long-term liabilities:					
Capital lease payable (note 6)	1,745,844	-	-	1,745,844	1,934,153
Total long-term liabilities	1,745,844	-	-	1,745,844	1,934,153
Total liabilities	2,197,221	577,728	-	2,774,949	2,741,208
Net assets:					
Invested in capital assets, net of related debt	211,006	9,992,167	290,053	10,493,226	10,682,520
Restricted for capital outlay	-	-	2,406,728	2,406,728	3,582,907
Unrestricted, available for appropriations	1,665,543	6,627,178	-	8,292,721	6,863,997
Total net assets	\$ 1,876,549	16,619,345	2,696,781	21,192,675	21,129,424

See accompanying notes to the basic financial statements.

COSTA MESA SANITARY DISTRICT
Enterprise Funds
Statement of Revenues, Expenses and Changes in Fund Net Assets
Year ended June 30, 2003
(with comparative totals for the year ended June 30, 2002)

			Nonmajor Enterprise Funds	Totals	
	Solid Waste	Liquid Waste		2003	2002
Operating revenues:					
Trash assessments	\$ 4,105,544	-	-	4,105,544	3,884,972
Sewer assessments	-	1,642,255	-	1,642,255	1,571,722
Permits and inspection fees	-	43,126	-	43,126	34,820
Connection fees	-	-	44,230	44,230	53,979
Other services	33,885	27,841	-	61,726	-
Investment recovery	2,332	-	-	2,332	12,967
Total operating revenues	4,141,761	1,713,222	44,230	5,899,213	5,558,460
Operating expenses:					
Solid waste disposal	2,356,566	-	-	2,356,566	2,289,609
Liquid waste disposal	-	906,596	-	906,596	854,911
Dump charges	1,927,050	-	-	1,927,050	1,756,721
Other	153,111	346,007	-	499,118	672,241
Depreciation	146,201	445,669	5,274	597,144	450,943
Total operating expenses	4,582,928	1,698,272	5,274	6,286,474	6,024,425
Operating income (loss)	(441,167)	14,950	38,956	(387,261)	(465,965)
Non-operating revenues (expenses):					
Investment income	64,318	269,102	85,271	418,691	531,421
Interest expense	(133,526)	-	-	(133,526)	(54,120)
Taxes	150,275	15,072	-	165,347	150,214
Other revenues (expenses)	-	-	-	-	3,083
Total non-operating revenues (expenses)	81,067	284,174	85,271	450,512	630,598
Income before capital contributions	(360,100)	299,124	124,227	63,251	164,633
Contributions:					
Contributed capital assets	-	-	-	-	131,680
Total contributions	-	-	-	-	131,680
Net income	(360,100)	299,124	124,227	63,251	296,313
Net assets at beginning of year, as restated (note 3)	2,236,649	16,320,221	2,572,554	21,129,424	20,833,111
Net assets at end of year	\$ 1,876,549	16,619,345	2,696,781	21,192,675	21,129,424

See accompanying notes to the basic financial statements.

COSTA MESA SANITARY DISTRICT

Enterprise Funds

Statement of Cash Flows

Year ended June 30, 2003

(with comparative totals for the year ended June 30, 2002)

			Nonmajor Enterprise Funds	Totals	
	Solid Waste	Liquid Waste		2003	2002
Cash flows from operating activities:					
Cash received from customers	\$ 4,144,984	1,716,165	48,070	5,909,219	5,607,092
Nonoperating miscellaneous revenue received	-	-	-	-	-
Cash payments to suppliers for goods and services	(4,461,000)	(994,573)	-	(5,455,573)	(5,283,670)
Net cash provided by (used for) operating activities	(316,016)	721,592	48,070	453,646	323,422
Cash flows from non-capital financing activities:					
Taxes received	150,275	15,072	-	165,347	150,214
Miscellaneous cash revenue	-	-	-	-	3,083
Net cash provided by (used for) non-capital financing activities	150,275	15,072	-	165,347	153,297
Cash flows from capital and related financing activities:					
Cash paid to acquire capital assets	(98,350)	(182,483)	-	(280,833)	(193,576)
Cash paid on capital lease	(281,182)	-	-	(281,182)	(54,120)
Net cash provided by (used for) capital and related financing activities	(379,532)	(182,483)	-	(562,015)	(247,696)
Cash flows from investing activities:					
Interest received	65,979	277,022	85,110	428,111	573,711
Net cash proved by (used for) investing activities	65,979	277,022	85,110	428,111	573,711
Net increase (decrease) in cash and cash equivalents	(479,294)	831,203	133,180	485,089	802,734
Cash and cash equivalents at beginning of year	2,309,005	6,314,220	2,260,063	10,883,288	10,080,554
Cash and cash equivalents at end of year	\$ 1,829,711	7,145,423	2,393,243	11,368,377	10,883,288

(Continued)

See accompanying notes to the basic financial statements.

COSTA MESA SANITARY DISTRICT

Enterprise Funds
Statement of Cash Flows
(Continued)

			Nonmajor Enterprise Funds	Totals	
	Solid Waste	Liquid Waste		2003	2002
Reconciliation of operating income (loss) to net cash provided by (used for) operating activities:					
Operating income (loss)	\$ (441,167)	14,950	38,956	(387,261)	(465,965)
Adjustments to reconcile operating income (loss) to net cash provided by (used for) operating activities:					
Depreciation	146,201	445,669	5,274	597,144	450,943
Disposal of capital assets	-	-	-	-	-
Nonoperating miscellaneous revenue received	-	-	-	-	-
Changes in assets and liabilities:					
(Increase) decrease in accounts receivable	2,658	(204)	-	2,454	4,937
(Increase) decrease in taxes receivable	565	(965)	-	(400)	(2,104)
(Increase) decrease in due from other governments	-	4,112	3,840	7,952	45,853
(Increase) decrease in other assets	-	52,360	-	52,360	6,989
Increase (decrease) in accounts payable	(23,829)	(24,737)	-	(48,566)	197,768
Increase (decrease) in due to other governments	-	239,519	-	239,519	69,142
Increase (decrease) in due to City of Costa Mesa	-	-	-	-	1,000
Increase (decrease) in deposits payable	200	(8,752)	-	(8,552)	11,619
Increase (decrease) in accrued liabilities	(644)	(360)	-	(1,004)	3,240
Total adjustments	125,151	706,642	9,114	840,907	789,387
Net cash provided by (used for) operating activities	\$ (316,016)	721,592	48,070	453,646	323,422

Non-cash investing, capital and financing activities:

During the years ended June 30, 2003 and 2002, assets of \$0 and \$35,950, respectively, were contributed to the District by developers. In addition, during the year ended June 30, 2002, assets of \$2,113,529 were acquired through a capital lease.

See accompanying notes to the basic financial statements.

COSTA MESA SANITARY DISTRICT

Notes to the Basic Financial Statements

Year ended June 30, 2003

(1) Summary of Significant Accounting Policies

The Costa Mesa Sanitary District (“District”) was incorporated in February 1944 pursuant to Division VI, Part 1 of the Health and Safety Code of the State of California (sometimes referred to as the Sanitary District Act of 1923). At the present time, the boundaries of the District extend into the cities of Costa Mesa and Newport Beach as well as unincorporated areas within the County of Orange.

On December 19, 1955, the District entered into an agreement with the City of Costa Mesa, pursuant to the authority contained in the Joint Exercise of Powers Act (Sections 6500-6513 of the Government Code). Currently, the City has been contracted by the District to provide maintenance services related to the sewer system.

The following is a summary of the District’s significant accounting policies:

(a) Fund Accounting

The basic accounting and reporting entity is a *fund*. A fund is defined as an independent fiscal and accounting entity with a self-balancing set of accounts, recording resources, related liabilities, obligations, reserves and equities segregated for the purpose of carrying out specific activities or attaining certain objectives in accordance with special regulations, restrictions or limitations. All funds of the District are enterprise funds.

The funds designated as major enterprise funds are determined by a mathematical calculation consistent with GASB Statement No. 34. The District reports the following major enterprise funds:

Solid Waste – This fund is used to account for the collection of trash assessment revenue, the cost of managing the refuse collection and recycling processes, and the cost of contract services provided to the District.

Liquid Waste – This fund is used to account for the collection of sewer assessment revenues, the cost of maintaining sewer lines and pump stations, and the cost of contract services provided to the District.

(b) Measurement Focus and Basis of Accounting

The proprietary fund types are accounted for on the economic resources measurement focus. Accordingly, all assets and liabilities are included on the Statement of Net Assets, and the reported net assets provides an indication of the historical net worth of the fund. Operating statements for proprietary fund types report increases (revenues) and decreases (expenses) in total historical net worth.

COSTA MESA SANITARY DISTRICT

Notes to the Basic Financial Statements

(Continued)

(1) Summary of Significant Accounting Policies, (Continued)

The District uses the accrual basis of accounting. Revenues are recognized when they are earned and expenses are recorded when the liability is incurred for receipt of the related goods and services.

Proprietary funds distinguish *operating* revenues and expenses from *non-operating* items. Operating revenues and expenses result from providing goods and services related to the fund's ongoing operations. The principal operating revenues of the District's enterprise funds are trash and sewer assessments, permits and inspection fees and connection fees. Operating expenses include the cost of services provided, general and administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. When both restricted and unrestricted resources are available for use, it is the District's policy to use restricted resources first, then unrestricted resources as they are needed.

(c) Investments

Investments are reported in the accompanying balance sheet at fair value. Changes in fair value that occur during a fiscal year are recognized as *investment income* reported for that fiscal year. *Investment income* includes interest earnings, changes in fair value, and any gains or losses realized upon the liquidation, maturity, or sale of investments.

(d) Cash Equivalents

For purposes of the statement of cash flows, cash equivalents are defined to include an investment in the City's cash and investment pool, as well as any direct investment in short-term, highly liquid investments that are both readily convertible to known amounts of cash or so near their maturity that they present insignificant risk of changes in value because of changes in interest rates, and have an original maturity date of three months or less. Investments in federal agency securities are not considered to be cash equivalents as defined above and, therefore, are excluded from the statements of cash flows.

(e) Capital Assets

Capital assets purchased by the District are capitalized at historical cost. Data reflected in the District capital asset records include estimates of original cost as determined by knowledgeable District personnel. Contributed capital assets, consisting primarily of donated subsurface lines dedicated to the District by sub-dividers, are recorded as contributed capital assets, which increases the net assets of the District. Such contributed capital assets are recorded at their fair market value at the time of donation.

COSTA MESA SANITARY DISTRICT

Notes to the Basic Financial Statements

(Continued)

(1) Summary of Significant Accounting Policies, (Continued)

Any single item purchased by the District with a cost greater than or equal to \$1,000 and an estimated useful life of greater than one year is capitalized and depreciated. Depreciation is charged to operations using the straight-line method based on the estimated useful life of the asset. The estimated useful lives are as follows:

Buildings	20 years
Improvements	20 years
Equipment	20 years
Subsurface sewer lines	60 years
Trash containers	15 years

(f) Comparative Data/Reclassifications

Comparative total data for the prior year have been presented only for individual enterprise funds in the fund financial statements in order to provide an understanding of the changes in the financial position and operations of these funds. Also, certain amounts presented in the prior year data have been reclassified in order to be consistent with the current year's presentation.

(2) Cash and Investments

Cash and investments held by the Sanitary District at June 30, 2003 consisted of the following:

Deposits	\$ (175,507)
Investments	<u>11,543,884</u>
Total cash and investments	<u>\$11,368,377</u>

The Costa Mesa Sanitary District is generally authorized under the state statute and local resolutions to invest in U.S. Treasury bills, U.S. Treasury notes, Federal agency securities, banker's acceptances, certificates of deposit, negotiable certificates of deposit, commercial paper, medium term notes, repurchase agreements, Local Agency Investment Fund of the State of California, Orange County Treasurer's Pool, asset-backed and mortgage-backed securities, money market mutual funds, and passbook savings account demand deposits.

COSTA MESA SANITARY DISTRICT

Notes to the Basic Financial Statements

(Continued)

(2) Cash and Investments, (Continued)

The District has also established guidelines for security purchases with investment limitations as follows: Bankers acceptances may not exceed 40% of the District's surplus money nor exceed 270 days maturity. Negotiable certificates of deposits may not exceed 30% of the District's surplus money. Commercial paper may not exceed 270 days maturity nor exceed 30% of the District's surplus funds. Medium term corporate notes may not exceed 30% of the District's surplus funds. The District may not invest more than 10% of its surplus funds in reverse repurchase agreements, and must always match its maturities to the reinvestment. The District may not invest more than 35% of its surplus money with the Orange County Treasurer's Pool. Asset-backed and mortgage-backed securities may not exceed 20% of the District's surplus money. The District may not invest more than 25% of its surplus in Federal Government sponsored Agency issues.

Under the California Government Code, a financial institution is required to secure deposits made by state or local governmental units by pledging securities held in the form of an undivided collateral pool. The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure District deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits.

Deposits of cities and other state or local governments are classified in three categories to give an indication of the level of custodial risk assumed by the entity at year end. Category 1 includes deposits that are insured or collateralized with securities held by the District or its agent in the District's name. Category 2 includes deposits collateralized with securities held by the pledging financial institution's trust department or agent in the District's name. Category 2 also includes deposits collateralized by an interest in an undivided collateral pool held by an authorized agent of depository and subject to certain regulatory requirements under State law. Category 3 includes deposits collateralized with securities held by the pledging financial institution, or by its trust department or agent but not in the District's name. Category 3 also includes any uncollateralized deposits.

<u>Form of Deposit</u>	<u>Category</u>			<u>Bank Balance</u>	<u>Carrying Amount</u>
	<u>1</u>	<u>2</u>	<u>3</u>		
Demand deposits	<u>\$5,522</u>	<u>-</u>	<u>-</u>	<u>5,522</u>	<u>(175,507)</u>

COSTA MESA SANITARY DISTRICT

Notes to the Basic Financial Statements

(Continued)

(2) Cash and Investments, (Continued)

Investments of cities and other state or local governments are classified in three categories to give an indication of the level of custodial risk assumed by the entity at year end. Category 1 includes investments that are insured, registered or are held by the District or its agent (other than the institution through which the District purchased the securities) in the District's name. Investments held "in the District's name" include securities held in a separate custodial or fiduciary account and identified as owned by the District in the custodian's internal accounting records. Category 2 includes uninsured and unregistered securities which are held in the District's name by the counterparty's trust department or agent. Category 3 includes uninsured and unregistered securities which are held by the counterparty, or the counterparty's trust department or agent, but not in the District's name. The counterparty is the party that acts as the broker-dealer agent of the District (the party that purchased the securities on behalf of the District). Category 3 includes all securities held by the broker-dealer of the District, regardless of whether or not the securities are being held in the District's name:

	<u>Category</u>			<u>Carrying</u>
	<u>1</u>	<u>2</u>	<u>3</u>	<u>Value</u>
Investments held by the District:				
Medium term corporate notes	\$ 741,778	-	-	741,778
Federal Agency Securities	<u>4,119,510</u>	<u>-</u>	<u>-</u>	<u>4,119,510</u>
	<u>\$4,861,288</u>	<u>-</u>	<u>-</u>	<u>4,861,288</u>
Investments held by the District not subject to categorization:				
Investment in State Investment Pool - LAIF				<u>6,682,596</u>
Total investments				<u>\$11,543,884</u>

The District is a voluntary participant in the Local Agency Investment Fund (LAIF) that is regulated by California Government Code Section 16429 under the oversight of the Treasurer of the State of California. The fair value of the District's investment in this pool is reported in the accompanying financial statements at amounts based upon the District's pro-rata share of the fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis. Included in LAIF's investment portfolio are collateralized mortgage obligations, mortgage-backed securities, other asset-backed securities, loans to certain state funds, and floating rate securities issued by federal agencies, government-sponsored enterprises, and corporations.

COSTA MESA SANITARY DISTRICT

Notes to the Basic Financial Statements

(Continued)

(3) Implementation of New Accounting Standard

During the year ended June 30, 2003, the District implemented GASB Statement No. 34, which changed the financial reporting model of local governmental units. As a result of GASB Statement No. 34, fund financials are required to be presented with a focus on the *major funds* of that local government. Previously, financial reporting for local governments had focused on reporting by *fund type*.

Under GASB Statement No. 34, retained earnings and contributed capital, the two components of equity in proprietary funds, are now combined and presented as net assets. The following summarizes the effects of the restatement to the beginning retained earnings as of July 1, 2001:

	<u>Solid Waste</u>	<u>Liquid Waste</u>	<u>Nonmajor Enterprise Funds</u>	<u>Total</u>
Retained earnings at beginning of year, as previously reported	\$2,382,397	11,324,359	2,419,526	16,126,282
To reflect prior years' contributed capital as net assets	<u>-</u>	<u>4,706,829</u>	<u>-</u>	<u>4,706,829</u>
Net assets at beginning of year, as restated	<u>\$2,382,397</u>	<u>16,031,188</u>	<u>2,419,526</u>	<u>20,833,111</u>

COSTA MESA SANITARY DISTRICT

Notes to the Basic Financial Statements

(Continued)

(4) Capital Assets

A summary of changes in capital assets follows:

	<u>Balance at July 1, 2002</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance at June 30, 2003</u>
Capital assets, not being depreciated:				
Construction in progress	\$ 300,011	130,123	-	430,134
Property rights	<u>4,025</u>	<u>-</u>	<u>-</u>	<u>4,025</u>
Total capital assets, not being depreciated	<u>304,036</u>	<u>130,123</u>	<u>-</u>	<u>434,159</u>
Capital assets being depreciated:				
Subsurface sewer lines	19,914,147	-	-	19,914,147
Building and improvements	346,520	-	-	346,520
Equipment	<u>2,651,735</u>	<u>98,350</u>	<u>-</u>	<u>2,750,085</u>
Total capital assets, being depreciated	<u>22,912,402</u>	<u>98,350</u>	<u>-</u>	<u>23,010,752</u>
Less accumulated depreciation for:				
Subsurface sewer lines	(10,046,980)	(410,681)	-	(10,457,660)
Building and improvements	(232,076)	(17,326)	-	(249,402)
Equipment	<u>(141,333)</u>	<u>(169,137)</u>	<u>-</u>	<u>(310,470)</u>
Total accumulated depreciation	<u>(10,420,389)</u>	<u>(597,144)</u>	<u>-</u>	<u>(11,017,532)</u>
Total capital assets, being depreciated, net	<u>\$12,796,049</u>	<u>(368,671)</u>	<u>-</u>	<u>12,427,379</u>

Depreciation expense was charged to functions of the District as follows:

Solid waste	\$146,201
Liquid waste	445,669
Sewer construction	-
Facilities revolving	<u>5,274</u>
Total depreciation expense	<u>\$597,144</u>

COSTA MESA SANITARY DISTRICT

Notes to the Basic Financial Statements

(Continued)

(5) Long-Term Liabilities

The following is a summary of changes in long-term liabilities for the year ended June 30, 2003:

	Balance at <u>July 1, 2002</u>	<u>Additions</u>	<u>Deletions</u>	Balance at <u>June 30, 2003</u>	Portion Due Within <u>One Year</u>	Portion Due Beyond <u>One Year</u>
Capital lease payable	<u>\$2,113,529</u>	<u>-</u>	<u>179,376</u>	<u>1,934,153</u>	<u>188,309</u>	<u>1,745,844</u>

(6) Capital Lease Payable

On July 12, 2001, the Costa Mesa Sanitary District entered into a 10 year lease agreement with the Municipal Finance Corporation to provide financing in the amount of \$2,200,000 for the acquisition of refuse containers. The lease provides a purchase option. The obligation is due in semi-annual principal and interest payments of \$140,591. Interest is computed at a stated rate of 4.92%.

Amount of future minimum lease payments required are as follows:

<u>June 30th</u>	<u>Business-Type Activities</u>	
	<u>Principal</u>	<u>Interest</u>
2004	\$ 188,310	92,872
2005	197,688	83,494
2006	207,534	73,648
2007	217,871	63,311
2008	228,722	52,460
2009	240,113	41,069
2010	252,072	29,110
2011	264,627	16,555
2012	<u>137,216</u>	<u>3,375</u>
Total	<u>\$1,934,153</u>	<u>455,894</u>

COSTA MESA SANITARY DISTRICT

Notes to the Basic Financial Statements

(Continued)

(7) Subsequent Events

On August 14, 2003, the Costa Mesa Sanitary District entered into an agreement with Municipal Finance Corporation to refinance the July 12, 2001 capital lease in the amount of \$1,887,171. The obligation will be due in semi-annual principal and interest payments of \$137,071 commencing on April 4, 2004. Interest is computed on the new lease at a stated rate of 3.65%.

SUPPLEMENTAL SCHEDULES

COSTA MESA SANITARY DISTRICT

Nonmajor Enterprise Funds

Combining Statement of Net Assets

June 30, 2003

	Sewer Construction	Facilities Revolving	Totals	
			2003	2002
<u>Assets</u>				
Current assets:				
Cash and investments	\$ 206,878	2,186,365	2,393,243	2,260,063
Cash with fiscal agent	-	-	-	-
Accounts receivable	-	-	-	-
Interest receivable	1,066	11,272	12,338	12,177
Taxes receivable	-	-	-	-
Due from other governments	-	1,147	1,147	4,988
Total current assets	207,944	2,198,784	2,406,728	2,277,228
Capital assets:				
Property rights	-	-	-	-
Subsurface sewer lines	-	316,421	316,421	316,421
Buildings and improvements	-	-	-	-
Equipment	-	-	-	-
Construction in progress	-	-	-	-
Total capital assets	-	316,421	316,421	316,421
Less accumulated depreciation	-	(26,368)	(26,368)	(21,095)
Net capital assets	-	290,053	290,053	295,326
Total assets	207,944	2,488,837	2,696,781	2,572,554
<u>Liabilities and Net Assets</u>				
Current liabilities:				
Accounts payable	-	-	-	-
Accrued liabilities	-	-	-	-
Deposits payable	-	-	-	-
Due to other governments	-	-	-	-
Due to the City of Costa Mesa	-	-	-	-
Capital lease payable	-	-	-	-
Total current liabilities	-	-	-	-
Long-term liabilities:				
Capital lease payable	-	-	-	-
Total long-term liabilities	-	-	-	-
Total liabilities	-	-	-	-
Net assets:				
Invested in capital assets, net of related debt	-	290,368	290,368	295,326
Restricted for capital outlay	207,944	2,198,469	2,406,413	2,277,228
Unrestricted, available for appropriations	-	-	-	-
Total net assets	\$ 207,944	2,488,837	2,696,781	2,572,554

COSTA MESA SANITARY DISTRICT
Enterprise Funds
Statement of Revenues, Expenses and Changes in Fund Net Assets
Year ended June 30, 2003

	Sewer Construction	Facilities Revolving	Totals	
			2003	2002
Operating revenues:				
Trash assessments	\$ -	-	-	-
Sewer assessments	-	-	-	-
Permits and inspection fees	-	-	-	-
Connection fees	-	44,230	44,230	53,673
Other services	-	-	-	-
Investment recovery	-	-	-	-
Total operating revenues	-	44,230	44,230	53,673
Operating expenses:				
Solid waste disposal	-	-	-	-
Liquid waste disposal	-	-	-	-
Dump charges	-	-	-	-
General and administration	-	-	-	-
Depreciation	-	5,274	5,274	5,274
Total operating expenses	-	5,274	5,274	5,274
Operating income (loss)	-	38,956	38,956	48,399
Non-operating revenues (expenses):				
Investment income	7,436	77,835	85,271	104,629
Interest expense	-	-	-	-
Taxes	-	-	-	-
Other revenues (expenses)	-	-	-	-
Total non-operating revenues (expenses)	7,436	77,835	85,271	104,629
Income before capital contributions	7,436	116,791	124,227	153,028
Contributions:				
Contributed capital assets	-	-	-	-
Total contributions	-	-	-	-
Net income	7,436	116,791	124,227	153,028
Net assets at beginning of year	200,508	2,372,046	2,572,554	2,419,526
Net assets at end of year	\$ 207,944	2,488,837	2,696,781	2,572,554